Stanford eCorner

Selling Customers -- Getting the Product Out

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Technology companies face four major development hurdles along the path to success: basic concept, the product, getting it to customers, and making money. Focusing on the last, the two prevalent business models for making money in the high tech market are advertising or partnering. After thorough analysis comparing the costs of different advertising strategies, the Paypal founders decided that, however unintuitive, giving each customer $10 for opening a new account was the cheapest method to obtain customers.

Transcript

But you know in parallel with raising money and recruiting people, we had actually forgotten a way to get the product out. And one of the biggest challenges in the technology can be observed on four different stages. One is, you know, a basic concept. Basic concept with the new online payments product. Second piece that's a technology is the product. How do you actually make it usable, get a user interface that actually works for people. Third question is how do you actually get customers? Let's assume you have a great product, great new technology. There's still the question how do you actually tell people about it? How do you get customers. And then the last question is how do you actually make money, which we weren't even worried about at that time. But the third question was a really challenging one it was how do you get customers? And the two basic models at the time of Silicon Valley were number one: you do advertising.

It was costing more and more and made less and less sense. We're driving from Powell to San Francisco one day, there were about 28 billboards on the highway and the costs had gone from $10000 a month for a billboard in '97 to $25000 a month in '98 to $100,000 a month in '99. And I remembered looking at them and most of them you could see for about 6 to 10 seconds and you couldn't understand anything it said. And that was one of the more cost-effective types of advertising one could do. The second type of business model was to work with a big partner and we thought that's what we should do. We should find a big partner who would take our product and disseminate it to the whole world. And one of the people at our company, Jack Selby managed to figure out, we were 22 people at this point in September of '99. He had figured out a way to get in to meet the chairman/CEO at HSBC, which is the second largest bank or third largest bank in the world that's based in London. They have about 100,000 employees. So it was an incredible demand.

So we flew over to London and we met with the chairman's hotel at breakfast and then we went in to see the CEO in this wood-paneled conference room and it was this unbelievable cultural disconnect. You know, one of the product people from our company was there and waving this Palm Pilot energetically. This is going to be the future payments. This is going to happen and the sort of mid-level executives who were there with the CEO told us that, yes they had just started advertising on television. And when we think of that, wasn't that really technologically advanced. And I remembered that evening Luke Nosek and I spent the whole evening time that, what a waste of time it had been to go to London and we needed to find a different way to get customers and we had to come up with a better way to get customers. So the classic even by then, the classic insanity of Silicon was basically selling dollar bills for $0.85. The business model of Silicon from 1999 according to the pundit was that, you know try to get a lot of customers in and you don't worry about making money. All you need to do is just offer

dollar bills for $0.85. People would buy it.

And of course, you know, being there to listen to all the wisdom, we decided, what the hell we'll do that. So anyone who would join PayPal would give $10 into the PayPal account and for anyone who would recruit, anyone who that person recruit, we give it additional $10 just for the referral. Just bring us another customer, which at the time even then got us plenty of flat. As the market started crashing, this was titled as the most insane scheme of all times. Of course, the one thing that these people didn't really calculate is that the average cost per customer was then $20. The nearest average cost of customer acquisition elsewhere for example with billboards or you know going door-to-door or sending people physical mail was higher. $65 to 100 was the next cheapest alternative was online click through ads for about $65. So basically, you're pretty clear as... Yes. The internal rationale might be crazy but everyone was crazier so we would outlast them all.

Yup. So skipping through a little, we were some time in March or April 2000, we started noticing these people from eBay... January 2000. January of 2000, people from eBay started sending us emails saying, "Hey, could we have a permission to include your logo in our auction?" And the first response that we had was like absolutely not, you know, what are you talking about? eBay was such a sketchy company. Sketchy company, already they were getting... Multilevel marketing people selling junk on the internet, I mean... It was just bad news. So, we told them no, go away. So I think for about two months we told them no. At some point we realized that there were more of them than of us.

And they did not need $20 to join. They were just coming in. So we had a change of heart.